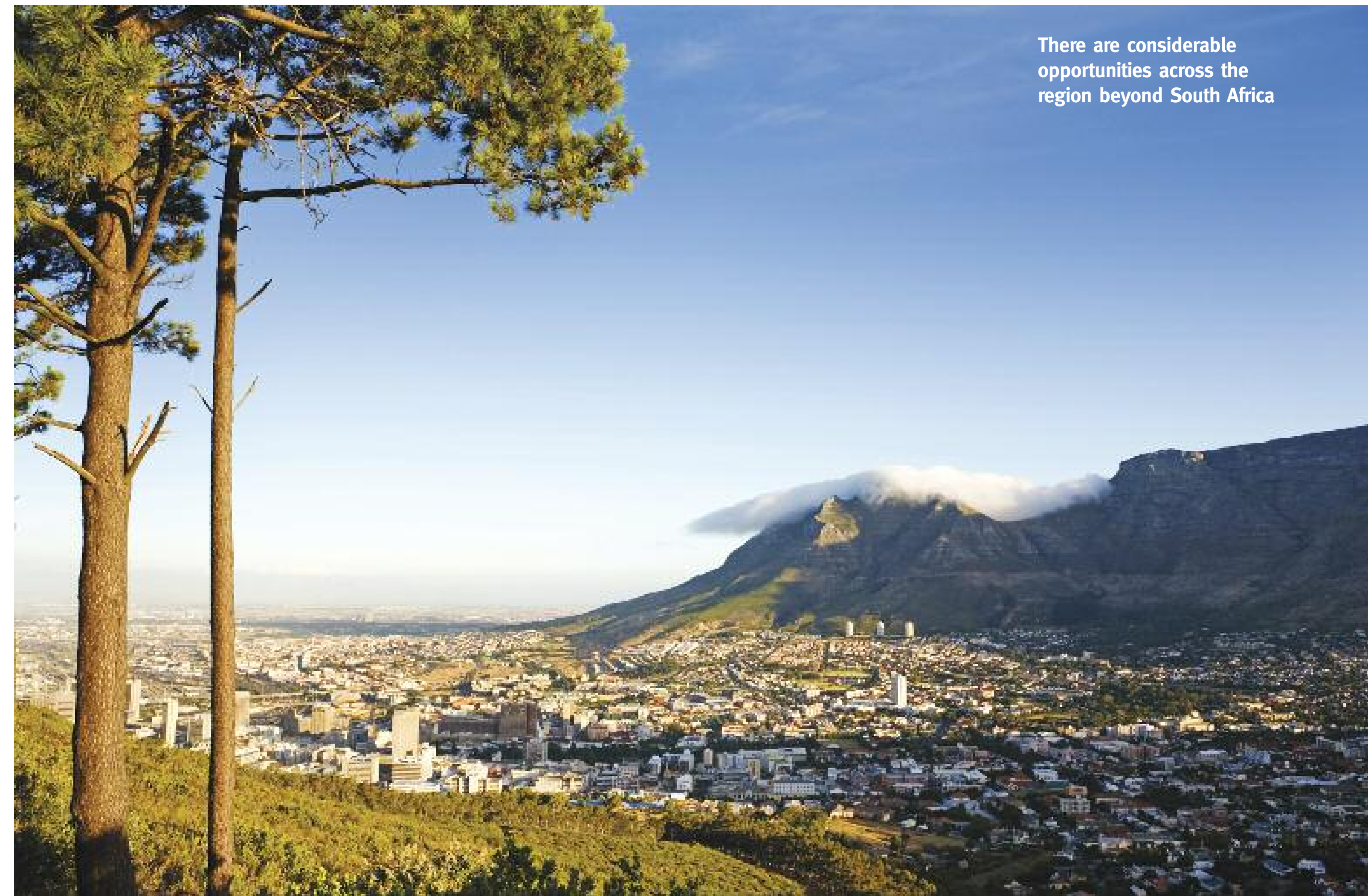
# Focus on Southern Africa



There are considerable opportunities across the region beyond South Africa

**The dominance of South Africa has overshadowed developments in neighbouring countries over the last decade. What are the main risks and management challenges now facing this region? By Rasaad Jamie**

The global financial crisis has unexpectedly raised the profile of Southern Africa as an area of economic opportunity. This is despite falling commodity prices and the political risk issues raised by events over the last year in Zimbabwe and Kenya and the ascent to power of the controversial Jacob Zuma in South Africa.

Many countries in the region are in a much better position than they were ten years ago, and now boast smaller current account and fiscal deficits, lower inflation, reduced debt burdens and increased foreign reserves. This is largely the result of three factors. First, the World Bank and IMF supervised structural adjustment programmes, which for a time produced significant discomfort and protest, but which nevertheless helped to strengthen policy frameworks.

The traditional lack of easy access to credit in the region was also a contributory factor, and last but not least, the conservative, heavy-handed approach to financial sector regulation meant local banks were largely insulated from the 'toxic' developments in the global financial system which now threaten the existence of banks elsewhere.

## Securing insurance cover

The opportunities produced by this situation, however, are tinged with impending challenges. Getting to grips with the political issues in the region is clearly a priority, but the cyclical nature of the insurance market means that one of the most straightforward aspects of corporate risk management – getting hold of appropriate cover – has suddenly become much harder.

The South African insurance market, in particular, had a tough time in 2008. Phil Gentry, a Partner in the Global Risk Solutions Division at Jardine Lloyd Thompson, points out that the local corporate insurance market suffered a number of high-profile losses last year. The combination of falling commodity prices and increased claims meant it was particularly hard for insurers providing cover to the country's flagship mining sector. Indeed, a significant number of insurers are in the process of withdrawing from that market globally, not only in Southern Africa.

Besides the losses in the South African mining industry, there were also a number of large industrial fires. "The result has been a significant hardening of the corporate property market," says Denis Ternent, Executive General Manager, Broking Services at Glenrand MIB, which is Jardine Lloyd Thompson's exclusive partner in Southern Africa. "Fortunately the casualty market has run relatively profitably for insurers and in consequence, this market is not seeing or experiencing increased rating levels."

In addition to imposing increased premium rates, deductible levels are also being increased in respect of clients that have suffered an adverse claims experience in recent years. In some instances, insurers have also reduced or placed certain cover restrictions on clients that are deemed to be a poor risk or that have failed to respond to insurers' previous requests to address risk improvement recommendations.

South African insurers have generally not experienced a reduction in treaty capacity with regards to corporate property, explains Ternent. "They are, however, being selective as to how they use their capacity. So where, for example, an insurer led with a 60 per cent line last year, they are only offering a 40 per cent line at renewal."

## Demonstrating risk management

There is a significantly increased focus on risk management in the South African market. "Insurers have been saying for some time now that clients need to manage their risk appropriately if they wish to receive the most favourable terms and conditions," continues Ternent. "If a client can't demonstrate to insurers that they have an active risk management process in place, they will be penalised in terms of higher deductibles, increased premium costs and possible restrictions in cover."

There are examples of companies that have incurred very few losses but are deemed to be poor risks by insurers and renewal has not been invited. As Ternent explains: "Insurers study loss trends and believe that it is a matter of time before the client suffers a large loss. So even in the case of a company with a favourable claims experience, unless it is perceived to have a well-managed risk management programme, insurers will not want to participate in that company's property programme."

Despite the tough stance taken by the conventional insurance market, Gentry does not see clients opting in any significant way for anything more exotic on the alternative risk transfer front than captives and other forms of self insurance. "People have talked about buying bonds but that has really not happened, and I don't see it happening in the current financial environment. So it comes down to working with the market," he says. "But it is certainly worthwhile for any corporate in the Southern African market to re-examine their risk transfer philosophy and consider if there is a better alternative."

Obtaining the necessary insurance cover, although difficult, is only one part of the story. The other part is making sure that in the process, you stay on the right side of local rules and regulations. With the obvious exceptions of the Angolan and Mozambican markets, which look to Portugal as a model, most of the insurance regulations in the region are generally standardised along Anglophone lines. This makes them similar to the South African market.

"All the countries peripheral to South Africa have updated their legislation over the last two to three years," explains Gerry Abrahamse, General Manager for Africa Division at Glenrand MIB. "Most of these markets now tend to follow similar practices utilising the same type of policy wordings, with notable exceptions being Angola and Mozambique. However, you do find that certain insurers within these countries, that have a connection via a shareholding to a South African insurer, will accommodate these wider wordings. Although insurance and reinsurance capacities vary from country to country, capacity is not normally a problem for the run of the mill risk, but can be

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problematic for the larger multinational and more complex risks."

### Spots and stripes

It is important, however, not to regard the region as one market. "Although there are common trends and common practices, Namibia, Botswana, Zimbabwe and Kenya are distinctly different markets," says Abrahamse, "with their own set of rules. All the major reinsurance companies such as Swiss Re and Munich Re are based in South Africa and there is very little legislation in neighbouring countries prohibiting local insurance companies from placing reinsurance outside of the market. But there are differences within these markets. For example, in Namibia, the option of first refusal of reinsurance business must be given to local companies (Namib Re) before the business may be offered outside the country."

Countries neighbouring South Africa such as Botswana, Namibia and Zimbabwe each have their own insurance acts, which prohibit non-admitted insurance. In some countries if there is insufficient capacity, or the risk cannot be written in that market, all you have to do is approach the local registrar via the intermediary used, and get permission to write the risk outside the country. "However, in other countries you have to get 'negative slips' from the local insurers to say that they can't write the business and only then can you export the cover outside the country," Abrahamse explains.

Most of the regional insurance acts are a little bit more specific in terms of non-admitted insurance. "They often require you to utilise a local intermediary," says Abrahamse. "This is their way to stop the 'suitcase brigade' flying in and flying out. Foreign brokers are simply not allowed to operate in these countries, unless they are licensed to do so."

When arranging insurance cover for African operations it is vital that risk managers ensure that the intermediary tasked with the job has a thorough understanding of the local insurance and legal requirements and provides adequate professional indemnity and fidelity cover. It must also understand the nuances of the business culture and language of that country.

### Keeping your eyes open

Compliance is critical to foreign companies when structuring insurance programmes in the region, according to Chris Louw, Global Insurance Manager at brewer SABMiller, which has extensive interests in Southern Africa. He stresses the need to understand local law and recommends using a local broker. It is essential that the local broker has risk engineering or modelling capability in order to understand the local environment risks.

"You need to know what the real political issues are," he notes, citing the example of the crisis in Zimbabwe, which he describes as "an unfortunate, but isolated example". He does not see countries such as South Africa, Angola or Mozambique as presenting big political risks. "From a risk management point of view, there are not massive concerns coming out of Southern Africa, but you have to go into the region with your eyes wide open," he says.

Crime is the big risk issue in South Africa, according to Louw. "So it is about how you structure your business and how you look after your staff," he says. "There isn't the threat of kidnap and ransom like you have in Latin America, but there is the risk that your managers will come to harm just by turning into their driveways. You have to think about how you are going to deal with a risk like that, particularly if your managers are foreign."

A corporate social responsibility programme is a good way of building real engagement with local communities and the issues that concern them. The knowledge and goodwill gained from such programmes constitute a form of indirect risk management. For example, SABMiller funds schools, organises medical projects and runs HIV/AIDS awareness programmes in the region.

"These things are vital. When you go into Southern Africa you have to be prepared to make a positive contribution to their development. SABMiller takes these projects very seriously," says Louw. The group also makes every effort to incorporate local industries and service providers into its regional supply chain. As he admits: "We have to – these are the people that drink our beer." RS

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## SHIFTING BALANCE

In 2007 South Africa accounted for around 82 per cent of the total gross premium income of the nearly $50 billion generated by the entire African continent, according to the latest available statistics from Swiss Re. However, the figures cited include life insurance business, which by itself accounts for the vast bulk (81 per cent) of the South African market's gross premium income. By comparison, the rest of Africa has no life insurance market to speak of.

However, the continent's non-life statistics tell a very different story. They show that the South African market accounted for only 54 per cent of the sector's gross premium income of $14.2 million in 2007. Less than a decade earlier, South Africa's proportion of African non-life premium income was closer to 80 per cent.

The difference between now and then is the result of two trends: the relatively slow growth in the South African non-life market in recent years and the rapid expansion in other regional markets such as Namibia, Botswana, Angola and Kenya. These trends are largely a result of the change in government economic policies and the influx of direct foreign investment into these countries.

In 2007, when the South African non-life insurance market grew by only 1.5 per cent, the Angolan market expanded by nearly 40 per cent and the Kenyan market by just over 25 per cent. Even the insurance markets of two of South Africa's economically more sedate neighbours, Botswana and Namibia, grew by 10 per cent and 7 per cent respectively.

# South Africa's risk rating

It is 15 years since the political transformation of South Africa and the charismatic figure of Nelson Mandela inspired and raised the expectations of the world, in terms of the social and economic potential of both South Africa and the Southern African region as a whole.

While South Africa has often been the focus of international attention, since 1994 the sense of euphoria and expectation has almost entirely dissipated. This is particularly the case in recent years, as government ministers face allegations of corruption and the administration appears at a loss as to how to deal with the HIV/AIDS epidemic, the high crime rate, xenophobic attacks on migrant workers and a shortage of essential skills. In terms of the regional picture, the crisis in Zimbabwe further exacerbates the political uncertainty.

But two developments, the provincial and national elections held on 22 April and the infrastructure investment and other preparations for the FIFA World Cup in 2010, provide the country with its greatest challenges yet, says Elizabeth Stephens, Head of Credit & Political Risk Analysis at Jardine Lloyd Thompson.

The ruling African National Congress party, led by Jacob Zuma, will form the next government, with the smooth preparation and staging of the World Cup being the most critical test of the new administration. Stephens says: "South Africa was selected because at the time it was considered the most able country on the continent to stage the tournament. Now we are at the stage where contingency plans may be put in place to stage the tournament elsewhere, because of concerns that South Africa might not be able to fulfil its obligations."

This reflects widespread concerns about the high crime rate and the deterioration in the general security situation. There have been large xenophobic protests which the police force was obviously unable to deal with. "So you have the question of calling in the army," she points out, "and having to deal with the message that is being sent out, if the armed forces of any country become involved in maintaining basic law and order."

However, it is not likely that South Africa will disintegrate into a Zimbabwe-type situation any time soon. Stephens says: "It obviously makes a difference that South Africa has fully functioning state institutions and a legal system. The organs of state as mechanisms of dispute resolution at all levels are there, even if they are flawed. The maintenance of the rule of law is hugely important."

But despite all the controversy surrounding Zuma, Stephens sees two positive aspects to his election as the president of South Africa. "He is a democratically elected leader with a strong mandate to govern. Also Zuma has been more credible in terms of his criticism of the behaviour of Robert Mugabe in Zimbabwe. The international community was deeply disappointed by the way Mbeki did not exert any pressure on Mugabe." RS

## WORLD RISK REVIEW™ RATINGS FOR SOUTHERN AFRICA

| | Botswana | Mozambique | Namibia | South Africa | Swaziland | Zimbabwe |
|---|---|---|---|---|---|---|
| Strikes, riots and civil commotion | 3 | 5 | 3 | 4 | 7 | 10 |
| Terrorism | 1 | 3 | 2 | 3 | 2 | 3 |
| War and civil war | 2 | 4 | 2 | 3 | 3 | 7 |
| Country economic risk | 4 | 6 | 4 | 4 | 5 | 9 |
| Currency inconvertability transfer risk | 3 | 6 | 4 | 4 | 5 | 10 |
| Sovereign credit risk | 4 | 7 | 5 | 5 | 6 | 9 |
| Expropriation | 4 | 4 | 4 | 4 | 6 | 9 |
| Contract agreement repudiation | 3 | 5 | 4 | 4 | 6 | 9 |
| Legal and regulatory risk | 4 | 6 | 4 | 4 | 6 | 10 |

## World Risk Review™

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The risk review rates nine perils in 197 countries and territories, captured under the broad categories of political violence, the trading environment and the investment environment.

The model is designed to enable companies to effectively identify the perils that may impact on their business and deliver an understanding of the relative level of risk associated with each peril, using a rating scale of 1 (low) to 10 (high).

The model incorporates independently verifiable data from 53 international sources, drawn from Europe, North America, Australia, Asia and the Middle East. The diversity and breadth of the data sources is intended to reduce, to the greatest extent possible, cultural bias, political influence and personal interpretation.

This approach contributes significantly to the robustness and integrity of the model and recognises that most country risk ratings available to business have traditionally been heavily influenced by Western bias reflecting the historical dominance of Western foreign investors and trading businesses.

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